

SPECIAL NOTICE

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Changes to the Manufacturing Machinery and Equipment Sales Tax Exemption

This Special Notice is being distributed to explain the 1996 changes to the statewide sales tax exemption for manufacturing machinery and equipment. The changes are contained in Substitute Senate Bill (SSB) 6656 (Chapter 173, Laws of 1996) and House Bill (HB) 2484 (Chapter 247, Law of 1996) and become effective on June 6, 1996.

Sales Tax Exemption for Repairs and Replacement Parts

Current law provides a sales and use tax exemption for machinery and equipment used directly in a manufacturing operation. Charges for installing qualifying machinery and equipment are also exempt from sales tax. However, the exemption does not apply to repair labor and parts, or to replacement parts that do not increase productivity, improve efficiency, or extend the useful life of the machinery and equipment.

SSB 6656, effective June 6, 1996, extends the exemption to include charges for repairing qualifying machinery and equipment, and repair and replacement parts with a useful life of one year or more. If the repair involves repair or replacement parts with a useful life of less than one year, then the labor charges (which are exempt) should be stated separately from the charge for the parts (which are taxable).

Sales Tax Exemption for Research and Development

HB 2484 extends the statewide sales tax exemption for machinery and equipment to include machinery and equipment used directly in a research and development (R&D) operation which is performed by a manufacturer or processor for hire. The legislation also creates a new sales and use tax exemption for materials incorporated into prototypes for the development of new aircraft parts, equipment, or modifications.

Research and development eligible for exemption is defined in RCW 82.63.010 as:

... activities performed to discover technological information, and technical and nonroutine activities concerned with translating technological information into new or improved products, processes, techniques, formulas, inventions, or software. The term includes exploration of a new use for an existing drug, device, or biological product if the new use requires separate licensing by the federal food and drug administration under chapter 21 C.F.R., as amended. The term does not include adaptation or duplication of existing products where the products are not substantially improved by application of the

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technology, nor does the term include surveys and studies, social science and humanities research, market research or testing, quality control, sale promotion and service, computer software developed for internal use, and research in areas such as improved style, taste, and seasonal design.

Unlike the high technology program enacted in 1995, HB 2484 does not require that the R&D be in the specific areas of advanced computing, electronic device technology, advanced materials, biotechnology, or environmental technology. Beginning on June 6, 1996, purchases of R&D machinery and equipment used in an R&D operation by a manufacturer will qualify for the sales tax exemption in the same manner as other machinery and equipment.

Requirements of the Exemption Program

The legislative changes effective June 6, 1996, do not alter the basic requirements for the machinery and equipment exemption. As with the current law passed in 1995, the machinery and equipment (including R&D equipment) must be sold to a manufacturer or processor for hire and must be used directly in a manufacturing operation.

The sales and use tax exemption does not include:

- ◆ Hand tools;
- ◆ Property with a useful life of less than one year;
- ◆ Building fixtures that are not integral to the manufacturing operation that are permanently affixed to and become a physical part of a building. This includes utility systems for heating, ventilation, air conditioning, communications, plumbing, or electrical.

To be considered “used directly” in a manufacturing operation or research and development operation, the machinery and equipment must:

- ◆ Act upon or interact with an item of tangible personal property;
- ◆ Convey, transport, handle, or temporarily store an item of tangible personal property at the manufacturing site;
- ◆ Control, guide, measure, verify, align, regulate, or test tangible personal property;
- ◆ Provide physical support for or access to tangible personal property;
- ◆ Produce steam or mechanical power for, or lubricate machinery and equipment;
- ◆ Produce another item of tangible personal property for use in the manufacturing operation or research and development operation;
- ◆ Place tangible personal property in the container, package, or wrapping in which the tangible personal property is normally sold or transported; or
- ◆ Is integral to research and development as defined in RCW 82.63.010.

The purchaser must provide the seller with a manufacturer’s sales and use tax exemption certificate at the time the sale takes place. A sample certificate is attached to this notice. The certificate has been

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revised to provide spaces for the new exemption categories. The certificate may be in the suggested format or any other form that provides the same information. No prior application is required to use the exemption. Both the buyer and seller must retain a copy of the certificate in their records for five years.

Purchasers are required to submit to the Department of Revenue an annual summary of purchases that qualify for the machinery and equipment exemption. The sample sales tax summary (shown at the end of this notice) is due on January 31st of the year following the calendar year the purchases were made. Buyers who make infrequent purchases of exempt items may file duplicate(s) of the exemption certificate(s) with the Department instead of filing an annual sales tax summary.

The expanded exemption also applies to use tax. Persons that use qualifying self-constructed machinery and equipment or machinery and equipment that was brought from a location outside of Washington are required to file an exemption certificate with the Department of Revenue within 60 days of when the item was first used in Washington. If there is a large amount of exempt equipment, the user can file an annual use tax summary with the Department instead of the certificate.

Unlike the sales and use tax exemption certificate, which can be used for both the sales and use tax exemptions, the annual summaries for sales tax and use tax are different forms. The annual summaries have been changed to reflect the new exempt categories.

Sales and Use Tax Exemption for Aircraft Parts

The new legislation also authorizes a sales and use tax exemption for materials incorporated into prototypes for the development of new aircraft parts, equipment, or modifications. The exemption is limited to businesses that have gross sales of less than \$20,000,000 per year. Eligible businesses can purchase up to \$100,000 in materials without the payment of sales tax. The maximum tax savings to a business is the amount of sales tax or use tax due on \$100,000. For example, if the sales tax rate where the \$100,000 purchase is made is 8.2 percent, the business would save the maximum amount of \$8,200 in sales tax. The exemption is effective on June 6, 1996.

Distressed Area Sales Tax Deferral/Exemption and B&O Credit Extended

The sales and use tax deferral/exemption program authorized by Chapter 82.60 RCW and the business and occupation tax credit authorized by Chapter 82.62 RCW provide tax relief in certain eligible areas. Currently, the basic definition for an eligible area is a county whose average rate of unemployment over the three prior years exceeds the statewide average by at least 20 percent.

Under this legislation, an additional definition for an eligible area is added. If the median household income for the three prior years is less than 75 percent of the state median household income the county will be classified as an eligible area. This additional definition will add two counties, Asotin and Whitman, to the distressed area programs. This legislation goes into effect on June 30, 1996.

To inquire about the availability of this document in an alternate format for the visually impaired, please call (360) 486-2342. Teletype (TTY) users please call 1-800-451-7985.



MANUFACTURER'S SALES AND USE TAX EXEMPTION CERTIFICATE

Type of Certificate

- ☐ Single Use Certificate
☐ Blanket Certificate (must be renewed every four years)
Invalid after _____

1. Buyer/User UBI/Revenue Registration No. _____
2. Name of Buyer/User _____
3. Address of Buyer/User _____
Street Address

City, State, Zip Code
4. Name of Seller _____

The buyer/user certifies that it is engaged in manufacturing or processing for hire activities and that the items purchased will be used directly in a manufacturing or processing for hire operation. A single use certificate must be used each time an exempt item is purchased. **The seller must keep a copy of the certificate for his/her records.**

To be considered "used directly" in a manufacturing operation or research and development operation, the machinery and equipment must:

- ◆ Act upon or interact with an item of tangible personal property;
- ◆ Convey, transport, handle, or temporarily store an item of tangible personal property at the manufacturing site;
- ◆ Control, guide, measure, verify, align, regulate, or test tangible personal property;
- ◆ Provide physical support for or access to tangible personal property;
- ◆ Produce steam or mechanical power for, or lubricate machinery and equipment;
- ◆ Produce another item of tangible personal property for use in the manufacturing operation or research and development operation;
- ◆ Place tangible personal property in the container, package, or wrapping in which the tangible personal property is normally sold or transported;
- ◆ Be integral to research and development as defined in RCW 82.63.010; or
- ◆ Be for repair and replacement parts or repair and cleaning labor for eligible items.

The sales and use tax exemption does not include:

- ◆ Consumable items;
- ◆ Hand-powered tools;
- ◆ Property with a useful life of less than one year;
- ◆ Building fixtures that are not integral to the manufacturing operation that are permanently affixed to and become a physical part of a building. This includes utility systems for heating, ventilation, air conditioning, communications, plumbing, or electrical.

➤ *This certificate is given with full knowledge of, and subject to, the legally prescribed penalties for fraud and tax evasion.*

Do not attach to the Combined Excise Tax Return.

Authorized Agent of Buyer/User (please print) _____

Authorized Signature _____ Title _____

Date _____

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